Supreme Court, U.S.
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92-No.1907

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

HUNTINGTON BREAKERS APARTMENTS, LTD.,
a partnership,
Petitioners,
vs.
C.W. DRIVER, a partnership,
Respondent.

PETITION FOR WRIT OF CERTIORARI
TO THE CALIFORNIA COURT OF APPEALS
FOURTH APPELLATE DISTRICT, DIVISION THREE

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED FOR REVIEW

Should an illegal side agreement that violates the principle of ***D'Oench, Duhme v. FDIC***, 315 U.S. 447 (1942) be enforcd by the Courts, merely because that illegality was not raised in an arbitration?

STATEMENT PURSUANT TO

SUPREME COURT RULE 29.1

Petitioner WILMORE CITY DEVELOPMENT, INC. has no parent or subsidiary company.

PARTIES TO THE PROCEEDING

All parties to the proceeding are listed in the caption.

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HUNTINGTON BREAKERS APARTMENTS, LTD., a partnership, et al.,
Petitioners,

vs.

C.W. DRIVER, a partnership,
Respondent.

PETITION FOR WRIT OF CERTIORARI

Petitioners HUNTINGTON BREAKERS APARTMENTS, LTD., a partnership; WILMORE CITY DEVELOPMENT, INC., and JOSEPH P. MAYER III (hereinafter "HUNTINGTON BREAKERS") respectfully pray that a writ of certiorari issue to review the opinion of the Court of Appeal, Fourth Appellate District of the State of California. A Petition for Review was denied by the California Supreme Court, by Order filed February 24, 1993 (Appendix A hereto).

OPINION BELOW

The Court of Appeal, Fourth Appellate District, of the State of California by its Opinion (Appendix B hereto) reversed an Order of the Superior Court of Orange County (Appendix C hereto) which had found a ***D'Oench Duhme*** type contract to be illegal. That reversal was based upon a recent opinion of the California Supreme Court, ***Moncharsh v. Heily and Blase*** (1992) 3 Cal.4th 1, 10 Cal.Rptr. 2d 183.

JURISDICTION

This Court has jurisdiction to review this matter pursuant to ***28 U.S.C.*** §2101(c) and Rule 10.1(b) of the Supreme Court Rules.

/ / / /

/ / / /

LEGAL PRINCIPLE INVOLVED

This case involves the primary issue of whether the illegality of a contract that violates the ***D'Oench Duhme (supra)*** rule, which requires the protection of federally insured financial institutions from the effect of illegal contracts, should take precedence over the waiver established by the California Supreme Court in its recent opinion in ***Moncharsh***.

STATEMENT OF THE CASE

In March of 1983, five people (Steven P. Semingson and his wife, Joseph P. Mayer III and his wife, and Daniel H. Young) joined together to form HUNTINGTON BREAKERS APARTMENTS, LTD., a California limited partnership ("BREAKERS"). A portion of that partnership interest was held in the name of another entity,

Wilmore City Development, Inc. On May 1, 1984, BREAKERS, as owner, entered into an American Institute of Architects (A.I.A.) form construction contract with C.W. DRIVER, a large general contractor in business since 1935, to construct for the five people a 342-unit apartment complex in Huntington Beach. The amount of that contract was $8.6 million. The project was financed by a federally insured and supervised lender Home Federal Savings & Loan. As a condition to DRIVER's execution of the A.I.A. form contract, DRIVER required all five individuals to also sign a side agreement entitled "Guarantee and Indemnity Agreement," prepared by DRIVER's attorney, Everett Maguire, which ostensibly increased the exposure of the S&L from $8.6 million to $11 million. This side agreement was not

a part of the S&L's file. The contractor represented to the lender that it would construct the project for the funds remaining in the loan.

After a dispute arose over the performance of the construction contract, DRIVER recorded a Mechanic's Lien, stopped work on the project and sued BREAKERS and the five individuals. DRIVER petitioned to compel arbitration under a hidden arbitration clause, buried in an attachment to the AIA form construction contract. The Guarantee and Indemnity Agreement contained no provision for arbitration. BREAKERS and the five individuals filed a cross-complaint against DRIVER for breach of contract, negligence, breach of fiduciary duty, fraud, negligent misrepresentation, declaratory relief, action on performance

and payment bonds, and injunction. The Superior Court granted DRIVER's motion to compel arbitration and ordered part of the action into arbitration. The guarantors were excluded from the arbitration. The arbitrators awarded DRIVER $3,021,502 consisting of contractual damages, pre-award interest, and costs and attorneys' fees. The total of the contractual damages awarded and the amounts paid to DRIVER under the contract exceeded the $8.6 million A.I.A. form contract amount. Also, there was no provision for attorneys fees in the AIA Form Agreement.

BREAKERS filed a Petition to Vacate Arbitration Award based on the illegality of the Guarantee and Indemnity Agreement and bias of the arbitrators. BREAKERS contended that the Guarantee and

Indemnity Agreement, which was prepared by DRIVER, concealed the true cost of construction from the construction lender, a federally insured institution, in violation of federal statutes and United States Supreme Court decisions. On July 12, 1991, the Superior Court granted BREAKERS' motion and found:

> "... that those portions of the contract document entitled 'Guaranty and Indemnity Agreement' ... that obligate the parties making that agreement to payment of any contractor-construction costs over and above the $8.6 million guaranteed maximum cost stated in the AIA Form Agreement

> constitute an illegal contract and are unenforceable."
> (Appendix C, p.8.)

DRIVER appealed that Order.

On July 30, 1992, prior to the presentation of oral argument by BREAKERS and DRIVER before the Court of Appeal, the California Supreme Court decided the case of ***Moncharsh***. That Court held that the arbitrator's award was not subject to judicial review because the issue of illegality had not been raised in an arbitration.

Based on the ***Moncharsh*** decision, the Court of Appeal in this case reversed the Superior Court's Order to Vacate Arbitration Award. (Opinion, Appendix B, p.4.) The California Supreme Court declined to review that opinion.

(Appendix A)

BREAKERS now petitions this Court for a review of that opinion by the Court of Appeal.

REASONS FOR GRANTING THE WRIT

SETTLEMENT OF IMPORTANT QUESTIONS OF LAW

There are important questions of law in this case that were not settled by the Court of Appeal's opinion. The principal issue of the appeal was the finding by the Superior Court that the Guarantee and Indemnity Agreement prepared by DRIVER was "illegal and unenforceable." The illegality involved issues of federal law, namely the violation of ***18 U.S.C.*** § 1014 as well as California Law (Fin. Code § 5308). It also involved established public policy in favor of full disclosure of a project's cost when the lender was a federally insured institution. That

public policy was affirmed in the recent Ninth Circuit case of ***Federal Savings & Loan Ins. Corp. v. Gemini Management*** 921 F.2d 241 (9th Circuit 1990), wherein that Court stated at page 244:

> "In 1942, the Supreme Court articulated a rule designed to implement a 'federal policy to protect [the FDIC] and the public funds which it administers against misrepresentations as to the securities or other assets in the portfolios of the banks which [the FDIC] insures or to which it makes loans.' ***D'Oench Duhme & Co. v. FDIC***, 315 U.S. 447, 457, 62 S.Ct.

676, 679, 86 L.Ed. 956 (1942). This policy is as sound today [1990] as it was in 1942, if not more so." (Emphasis added)

The 9th Circuit Court in ***Gemini*** then brought the ***D'Oench*** doctrine up to date (1990) by stating at page 245:

"These words are particularly meaningful today. As the Savings and Loan crisis in which this nation is mired continues to unfold, regulators are discovering abuses the *D'Oench* Court could not have imagined or predicted. The FSLIC's

> ability to evaluate the financial condition of troubled thrift institutions depends, now more than ever, upon the protective shield of *D'Oench*.
>
> "We cannot condone a transaction with the capacity to deceive the banking regulators, nor can we reward [the parties] for their creative and deceptive paperwork."

The Court of Appeal did not even consider the issue of whether the Guarantee and Indemnity Agreement was illegal as a matter of law. That issue had been submitted and argued to that

Court. It reasoned, pursuant to ***Moncharsh***, that since it was contended by BREAKERS that the guarantee was severable, and because illegality had not been raised as an issue during arbitration, "[BREAKERS'] failure to raise the issue of illegality precluded any future judicial review." (Opinion, Appendix B, p.18.)

However, the illegality described in ***Moncharsh*** was not the same as the illegality that is the subject of this Petition. First, there were no federal questions involved, and secondly, statutory rights of non-parties were not an issue. By not addressing the issue of illegality, the Court of Appeal erroneously applied the rule in ***Moncharsh*** to the facts of this case.

Even though the California Supreme

Court in ***Moncharsh*** suggested that, under the circumstances of that case, illegality of a portion of a contract is waived by the affected party if not raised during arbitration, Petitioners submit that the result should not be the same when illegality is based on a violation of federal statutes and recognized public policy.

ILLEGALITY OF THE GUARANTEE AND INDEMNITY AGREEMENT SHOULD HAVE BEEN CONSIDERED BY THE COURT OF APPEAL BECAUSE IT WAS THE PRINCIPAL ISSUE OF THE APPEAL

The basis for the Superior Court's July 12, 1991 Order Vacating Arbitrator's Award (Appendix C) was a finding cited in the Court of Appeal's opinion (Appendix B, p. 7) as follows:

"In its judgment, the

> court found 'that those portions of the contract document entitled 'Guaranty [sic] and Indemnity Agreement' . . . that obligate the parties making that agreement to the payment of any contractor-construction costs over and above the $8.6 million guaranteed maximum cost stated in the AIA Form Agreement constitute an illegal contract and are unenforceable."
>
> [Emphasis added.]

It was this "finding" of illegality that was the basis of the appeal by

DRIVER. However, the Court of Appeal did not address this issue in its opinion and did not articulate any reasons for not addressing this issue. In reading the opinion, however, it appears that the Court considered the issue moot, since the illegality was deemed severable, and it had not been raised during arbitration.

The Court of Appeal (Appendix B, p.18) stated:

> "Here, Breakers contended, and continues to contend, that the guarantee was severable, so that other provisions could survive a finding that portions of the guarantee are illegal. Thus, its failure to

raise the issue of illegality precluded any future judicial review."

THE *MONCHARSH* OPINION, RENDERED IN THE CONTEXT OF WHAT THE CALIFORNIA SUPREME COURT DETERMINED TO BE A PRIVATE DISPUTE, OUGHT NOT EXTEND TO CASES REQUIRING JUDICIAL PROTECTION OF STATUTORILY-BASED NON-PARTY PUBLIC INTERESTS

The California Supreme Court has, for more than fifty years, declared as illegal and unenforceable contracts between private party litigants when the Court perceives that the Court must be the source of protection for the public's interest, regardless of the desires of the litigants or the procedural history of the cases before the Court. (See

McAllister v. Drapeau (1939) 14 Cal.2d 102, 92 P.2d 911.)

Accordingly, the statutory interest of the public, and of financial institutions which serve the public interest, are not matters that can be relegated to the voluntary submission of the dispute to arbitrators. The public was not party to that submission, yet the public must be protected by judicial deterrence of illegal conduct.

In ***McAllister v. Drapeau***, the California Supreme Court held that an undisclosed "secret" side agreement between the private contracting parties "violates the basic public policy expressed in the act [The Home Owners' Loan Act of 1933]" (***Id.*** at 109) and "is tantamount to a fraud on the [government]". (***Id.*** at 111).

In ***Young v. Hampton*** (1951) 36 Cal.2d 799, 228 P.2d 1, 19 A.L.R.2d 830, the California Supreme Court protected the non-party public interest. The ***Young*** Court, citing ***McAllister (supra)*** and other cases, stated that "the policy announced in these decisions of affording the protection of the law to those whom the federal loan statutes are designed to benefit is a sound one..." (***Id.*** at 805.)

Another concurrent construction case, ***Pitts v. Highland Construction*** (1953) 115 Cal.App.2d 206, 252 P.2d 14, consistently held that in cases involving the public interest in honest dealing with public financing (or publicly guaranteed bank financing), California courts will not enforce side agreements that require payment of higher amounts than the amount disclosed to the lending

bank as the full cost of the project. Perhaps because none of ***McAllister, Young*** and ***Pitts*** cases involved arbitration, the doctrine of public policy protection for which they stand was not considered by the California Supreme Court in its ***Moncharsh*** opinion. Yet, because of today's near-exclusive predominance of arbitration clauses in the printed form contracts published by professionals in the building industry, this Court should anticipate that the vital ***McAllister, Young*** and ***Pitts*** line will die if the ***Moncharsh*** opinion can be taken to say that courts will no longer review contracts that are partially illegal (i.e. the "secret" part prepared by the contractor builder and not disclosed to the housing lender). This Court can and should expressly recognize that the

Moncharsh opinion does not address and should not be precedent for "illegality" cases involving statutorily based public policy interests of non-parties. The modern cases in this area are arising through arbitration.

The case law protecting the public interest, in this area of bank lending for housing, falls squarely within the prospective exception recognized in ***Moncharsh*** (at page 53) that judicial review may be had for protection of a right having "an explicit legislative expression of public policy." (*Id.*) Therefore, when the exception involves not a "party's statutory rights" (*Id.*) but the statutory rights of the non-party public, the basis for ***Moncharsh*** should not apply.

Notwithstanding ***Moncharsh***, an

arbitration award should not be based on an agreement that violates federal law and policy. (See ***Perez v. Campbell*** (1971) 402 U.S. 637, 91 S.Ct. 1704, 1711, 29 L.Ed. 2d 233, 242; ***Bothman v. Ukiah*** (1989) 216 Cal.App.3d 1395, 1408, 265 Cal.Rptr. 539.)

CONCLUSION

Petitioners HUNTINGTON BREAKERS believe that the current economic situation relating to illegal contracts that defraud federally insured financial institutions should warrant the interest of this Court sufficiently to grant certiorari.

A review of recent action by this Court involving the ***D'Oench Duhme*** doctrine indicates that this Court is interested in not diluting that doctrine in any way. Examples are Docket No. 92-

428 ***Graff v. Bank One***, Texas N.A. (61 LW 3288, review denied January 11, 1993, 61 LW 3477), Docket No. 92-840 ***Pacific Southwest Bank F.S.B. v. Bradley,*** (61 LW 3447, review denied March 9, 1993), Docket No. 92-935 ***Ward v. Resolution Trust Corp.*** (61 LW 3512), and Docket No. 91-1856 ***Triple M Drilling Co. v. Seider,*** (61 LW 3002; review denied October 5, 1992, 61 LM 3256).

The Court of Appeal, by following ***Moncharsh*** in this case, disregarded the overriding requirement of protecting federally insured financial institutions. Petitioners submit that this Court should grant this Petition.

Respectfully submitted,

CALLAHAN, McCUNE & WILLIS

GEORGE W. COLEMAN

APPENDIX A

Supreme Court
FILED
Feb 24 1993
Robert Wandruff Clerk
H. Cruz
Deputy

Fourth Appellate District,
Division Thre
No. G011323
S030278

IN THE SUPREME COURT OF
THE STATE OF CALIFORNIA

IN BANK

C. W. DRIVER, Appellant

v.

HUNTINGTON BREAKERS APARTMENTS LTD. Et Al., Appellants

And Companion Case

Appellants' petition for review DENIED.

/LUCAS/

Chief Justice

APPENDIX B

COURT OF APPEAL
4TH DISTRICT
DIVISION 3
NOV 6 1992

Deputy Clerk

NOT TO BE PUBLISHED

IN THE COURT OF APPEAL

OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT,

DIVISION THREE

C.W. DRIVER,

Plaintiff and Appellant,

v.

HUNTINGTON BREAKERS APARTMENTS,

LTD etc.,

Defendants and Appellants.

G011323

(Consol. with G011659)

(Super. Ct. No. 477394)

OPINION

APPEAL from a judgment of the Superior Court of Orange County, Robert A. Knox, Judge. Reversed.

Maguire, Toghia & Orbach, Everett W. Maguire, Stephen L. Chesney, Robyn K. Cossack and Jay Sherman for Plaintiff and Appellant.

Callahan, McCune & Willis, George W. Coleman and Steven A. O'Rourke for Defendants and Respondents.

* * *

In 1986, the superior court granted C. W. Driver's motion to compel arbitration of a contract dispute. Four years and over 130 hearings later, three arbitrators unanimously awarded Driver $3,021,502. However, in 1991 the superior court vacated the award, based upon the alleged illegality of a collateral guarantee executed by Huntington Breakers Apartments, Ltd.[1]

Driver seeks reversal of an order granting Breakers' petition to vacate the arbitration award. Breakers appeals an

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[1] Driver is a California general partnership and a building contractor composed of three California corporations, C.W. Driver, Inc., John Tyler, Inc. and Somers Financial, Inc. (collectively Driver). Huntington Breakers apartments, Ltd. is a California limited partnership with two general partners, Wilmore City Development, Inc. (Wilmore), a California corporation, and Joseph P. Mayer (Mayer) (collectively Breakers).

order granting Driver's motion to strike its memorandum of costs in which it sought $2,262,759.41 in fees and costs.

The Supreme Court's decision in Moncharsh v. Heily & Blase (1992) 3 Cal.4th 1 requires reversal.

FACTS

This case arises out of a dispute over the construction of a 342-unit apartment complex in Huntington Beach. Driver, a contractor, and Breakers, real estate developers and the owners of the property, entered into an American Institute of Architects (AIA) form construction contract on May 4, 1984, pursuant to which Driver agreed to construct the apartment complex. The contract incorporated "general conditions" by reference, providing for

arbitration of contractual disputes. At the time of the execution of the contract, Driver and Breakers entered into a guarantee and indemnity agreement. The contract itself provided that the maximum cost to the owner, Breakers, including the cost of Driver's work and contractor's fee, was guaranteed not to exceed $8,600,000. However, the guarantee and indemnity agreement, prepared by Driver, provided that Breakers' maximum obligation could not exceed $11,000,000 plus increased construction costs which might result from revisions and modifications required by the city or from changes and extra work requested by the owner or lender.

A dispute arose over the performance of the construction contract and, on December 26, 1985, Driver filed a

complaint for foreclosure of mechanic's lien and a petition to compel arbitration and stay the action pending the outcome of that arbitration. Breakers and others filed a cross-complaint against Driver for breach of contract, negligence, breach of fiduciary duty, fraud, negligent misrepresentation, declaratory relief, action on performance bond and payment bond, and for injunction. The superior court severed a portion of the litigation and ordered it into arbitration. Arbitration began shortly thereafter but ultimately involved more than 130 days of hearings over a period of four years[2], concluding in a unanimous

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2 This is the second time we have reviewed aspects of this apparently never-ending case. In a prior unpublished opinion (G009921), we affirmed the dismissal of Breakers' second amended cross-complaint against other parties for failure to serve the

award for driver of $1,500,535, plus pre-award interest of $304,398 and costs and attorney's fees of $1,141,469, for a total award of $3,021,502.

Thereafter, Breakers filed a petition to vacate the award, contending the contract was illegal, that the arbitrators were biased, and that improper parties were ordered to participate in the arbitration. On April 8, 1991, the superior court granted Breakers' motion to vacate the award on the ground that the contract was illegal. In its judgment, the court found 'that those portions of the contract document entitled 'Guaranty [sic] and Indemnity

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cross-complaint within three years. This case is not model example of "the purpose of arbitration -- to provide a speedy and inexpensive trial before commercial specialists." (Green v. Mt. Diablo Hospital Dist. (1989) 207 Cal.App.3d 63, 70.)

Agreement' . . . that obligate the parties making that agreement to the payment of any contractor-construction costs over and above the $8.6 million guaranteed maximum cost stated in the AIA Form Agreement constitute an illegal contract and are unenforceable." Driver's appeal followed.

Breakers filed a motion seeking attorney's fees and costs. The court granted Driver's motion to strike the memorandum of costs and Breakers' appeal followed.

DISCUSSION

Following the briefing in this matter, we permitted the parties to file supplemental briefs on the applicability of the Supreme Court's decision in Moncharsh v. Heily & Blase, supra, 3

Cal.4th 1 (hereafter Moncharsh), which was decided July 30, 1992.[3] In Moncharsh, an attorney terminated his employment with a law firm, but continued to represent clients who had signed retainer agreements with his former firm. A dispute arose regarding the firm's quantum meruit claim for fees and a percentage of the fees pursuant to a fee-splitting provision of the former employment contract. The parties submitted the dispute to arbitration and, although the attorney claimed the fee-splitting provision was illegal, the arbitrator ruled in favor of the law firm and the trial court granted the firm's

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3 Of course, the rule in Moncharsh is binding upon this court and must be applied retroactively to this case. (See Moradi-Shalal v. Fireman's Fund Ins. Companies (1988) 46 Cal.3d 287, 305; Peterson v. Superior Court (1982) 31 Cal.3d 147, 151-152.)

petition to confirm the award. (Id. at pp. 6-8.) The Court of Appeal affirmed, recognizing the general rule prohibiting review of the merits of an arbitrator's award, and the Supreme Court affirmed. (Id. at p. 8.)

The Supreme Court noted that in a private or nonjudicial arbitration, the scope of the arbitration is a matter of agreement between the parties and the arbitrator's powers are limited by agreement or stipulation. (Moncharsh, supra, 3 Cal.4th at p. 8; see also Ericksen, Arbuthnot, McCarthy, Kearney & Walsh, Inc. v. 100 Oak Street (1983) 35 Cal.3d 312, 323; O'Malley v. Petroleum Maintenance Co. (1957) 48 Cal.2d 107, 110.)[4] The court noted, in a detailed

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[4] At oral argument, Breakers' counsel argued for the first time that an April 14, 1986 letter to Driver's counsel

analysis of the history of arbitration, that "the Legislature has expressed a 'strong public policy in favor of arbitration as a speedy and relatively inexpensive means of dispute resolution.'" (Id. at p. 9. quoting Ericksen, Arbuthnot, McCarthy, Kearney & Walsh, Inc. v. 100 Oak Street, supra, at p. 322.) Thus, 'it is the general rule that parties to a private arbitration impliedly agree that the arbitrator's decision will be both binding and final." (Moncharsh, supra, at p. 9, fn. omitted.) for this reason, 'an award reached by an

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constituted a stipulation that Breakers did not waive its right to appeal by participating in the arbitration. The argument is disingenuous at best. First, there was no such stipulation. And second, the letter referred only to participation by the general partners, Wilmore and Mayer, whom Beakers now contends were erroneously ordered into arbitration.

arbitrator pursuant to a contractual agreement to arbitrate is not subject to judicial review except on the grounds set forth in [Code of Civil Procedure] sections 1286.2 (to vacate) and 1286.6 (for correction). Further, the existence of an error of law apparent on the face of the award that causes substantial injustice does not provide grounds for judicial review. [¶] [T]he normal rule of limited judicial review may not be avoided by a claim that a provision of the contract, construed or applied by the arbitrator, is 'illegal,' except in rare cases when according finality to the arbitrator's decision would be incompatible with the protection of a statutory right." (Id. at p. 33.)

Code of Civil Procedure section 1286.2 provides: "Grounds for vacation

of award [¶] [T]he court shall vacate the award if the court determines that: [¶] (a) The award was procured by corruption, fraud, or other undue means; [¶] (b) There was corruption in any of the arbitrators; [¶] (c) The rights of such party were substantially prejudiced by misconduct of a neutral arbitrator; [¶] (d) The arbitrators exceeded their powers and the award cannot be corrected without affecting the merits of the decision upon the controversy submitted; or [¶] (e) the rights of such party were substantially prejudiced by the refusal of the arbitrators to postpone the hearing upon sufficient cause being shown therefor or by the refusal of the arbitrators to hear evidence material to the controversy or by the conduct of the arbitrators contrary to the provisions of this

title." None of the statutory grounds for vacating the award exists here. Thus, the order vacating the award must be reversed.

Moreover, a second reason exists for reversing the order. In Moncharsh, the Supreme Court discussed the issue of whether illegality of a contract permits judicial review. There, the attorney contended the arbitrator's award was subject to judicial review because the fee-splitting provision of the agreement was illegal and in violation of public policy. But he did not contend the illegal provision rendered the entire contract or the agreement to arbitrate illegal." Accordingly, his illegality claim was an arbitrable one, and he did not waive the issue by failing to object to arbitration on this ground."

(Moncharsh, supra, 3 Cal.4th at p. 29.)

"If a contract includes an arbitration agreement, and grounds exist to revoke the entire contract, such grounds would also vitiate the arbitration agreement. Thus, if an otherwise enforceable arbitration agreement is contained in an illegal contract, a party may avoid arbitration altogether." (Ibid.; see also California State Council of Carpenters v. Superior Court (1970) 11 Cal.App.3d 144, 157.) "By contrast, when -- as here-- the alleged illegality goes to only a portion of the contract (that does not include the arbitration agreement), the entire controversy, including the issue of illegality, remains arbitrable." (Moncharsh, supra, 3 Cal.4th at p. 71; American & Nat. etc. Baseball Clubs v.

Major League Baseball Clubs v. Major League Baseball Players Assn. (1976) 59 Cal.App.3d 493, 498.)

As in Moncharsh, Breakers does not contend the alleged illegality constituted grounds to revoke the entire contract nor that the alleged illegality voided the arbitration clause of the contract. "Accordingly, the legality of the . . . provision was a question for the arbitrator in the first instance." (Moncharsh, supra, 3 Cal.4th at p. 30) The issue of the illegality of the provision is waived if it is not raised before the arbitrator. "Any other conclusion is inconsistent with the basic purpose of private arbitration, which is to finally decide a dispute between the parties. Moreover, we cannot permit a party to sit on his rights, content in

the knowledge that should he suffer an adverse decision, he could then raise the illegality issue in a motion to vacate the arbitrator's award. A contrary rule would condone a level of 'procedural gamesmanship' that we have condemned as 'undermining the advantages of arbitration.'" (Id. at p. 30, quoting Ericksen, Arbuthnot, McCarthy, Kearney & Walsh, Inc. v. 100 Oak Street, supra, 35 Cal.3d at p. 323; see also Christensen v. Dewor Developments (1983) 33 Cal.3d 778, 783-784.) As the Supreme Court stated, "unless a party is claiming (i) the entire contract is illegal, or (ii) the arbitration agreement itself is illegal, he or she need not raise the illegality question prior to participating in the arbitration process, so long as the issue is raised before

the arbitrator. Failure to raise the claim before the arbitrator, however, waives the claim for any future judicial review. " (Moncharsh, supra, at p. 31, emphasis added.)

Here, Breakers contended, and continues to contend, that the guarantee was severable, so that other provisions could survive a finding that portions of the guarantee are illegal. Thus, its failure to raise the issue of illegality precluded any future judicial review. (Moncharsh, supra, 3 Cal.4th at p. 31; see also Loving & Evans v. Blick (1949) 33 Cal.2d 603, 609; All Points Traders, Inc. v. Barrington Associates (1989) 211 Cal.App.3d 723, 738.)[5]

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5 In view of our holding, the arbitration award will be reinstated. Therefore, we do not address Breakers' claim for attorney's fees and costs. However, because we cannot conclude no

Breakers filed not one, but three separate petitions to vacate the arbitration award, alleging illegal contract, improper parties, and arbitrators' bias. In its order vacating the arbitration award, the trial court vacated the award on the ground of illegal contract, and concluded the petitions on the grounds of improper parties and bias were moot. Therefore, Breakers contends the issues raised in the latter petitions are not ripe for review by this court. However, based on the record, we may dispose of those

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reasonable attorney would find Breaker's appeal was without merit, Driver's request for sanctions for a frivolous appeal is denied. (In re Marriage of Flaherty (1982) 31 Cal.3d 637, 650; see also Portola Hills Community Assn. v. James (1992) 4 Cal.App.4th 289, 294.)

issues as a matter of law. Breakers' petition to vacate the award on the ground of improper parties was based upon its contention that its general partner, Wilmore and Mayer, were guarantors only. However, general partners of a limited partnership are bound by an arbitration agreement between the partnership and a third party. (Keller Construction Co. v. Kashani (1990) 220 Cal.App.3d 222, 229.) Moreover, in pleadings filed in the superior court, Breakers admitted that Wilmore and Mayer were parties to the arbitration agreement. Accordingly, there was no basis for the court to vacate the arbitration award on the ground that improper parties were ordered to participate in the arbitration.

Similarly, there is no merit to Breakers' contention that the award

should be vacated because of arbitrators' bias. The petition did not identify which arbitrators were allegedly biased. The sole basis for the petition on this ground was that Warren Driver, who has a major financial interest in Driver, is also a member of the American Arbitration Association panel of arbitrators and is on its regional advisory committee. However, "a personal relationship (acquaintance) between an arbitrator and a party to the arbitration does not require vacation of an award for possible bias. [Citation.] Because arbitrators are selected for their familiarity with the type of business dispute involved, they are not expected to be entirely without business contacts in the particular field. [Citation.] The fact that an arbitrator and a party to the

arbitration are members of the same professional organization 'is in itself hardly a credible basis for inferring even an impression of bias.'" (Ray Wilson Co. v. Anaheim Memorial Hospital Assn. (1985) 166 Cal.App.3d 1081, 1087-1088, quoting San Luis Obispo Bay Properties, Inc. v. Pacific Gas & Elec. Co. (1972) 28 Cal.App.3d 556, 567.) Thus, Breakers' contention that the award should be vacated because of arbitrators' bias is unsupported.

DISPOSITION

As to Drivers' appeal, the order granting the petition to vacate the arbitration award is reversed. As to Breakers' appeal, the order denying the claim for attorney's fees and costs is affirmed. Driver shall recover its costs

on appeal.

/s/ MOORE

MOORE, J.

WE CONCUR:

/s/ CROSBY
CROSBY, ACTING P.J.

/S/ WALLIN
WALLIN, J.

APPENDIX C

FILED
JUL 12 1991
GARY L. GRANVILLE, COUNTY CLERK
By _____ Deputy

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Attorneys for Defendants
HUNTINGTON BREAKERS APARTMENTS, LTD.,
a Partnership, et al

SUPERIOR COURT OF THE STATE OF CALIFORNIA
FOR THE COUNTY OF ORANGE

C. W. DRIVER, a Partnership,	)	CASE NO. 477 394
	)	DIFFERENTIAL CASE MANAGEMENT PROGRAM
Plaintiff,	)	
vs.	)	Judge Robert A. Knox
HUNTINGTON BREAKERS APARTMENTS, LTD., a Partnership, et al,	)	**ORDER VACATING ARBITRATION AWARD**
Defendants.	)	
AND RELATED CROSS ACTIONS	)	

The following listed matters came on for hearing on March 7, 1991 in Department "71" of the above-entitled court, the Honorable Robert A. Knox presiding:

1. Petition of Defendants HUNTINGTON BREAKERS APARTMENTS, LTD., WILMORE CITY DEVELOPMENT, INC., and JOSEPH P. MAYER III (collectively hereinafter "HUNTINGTON BREAKERS") to Vacate Arbitration Award (Illegal Contract)
2. Petition of Defendants HUNTINGTON BREAKERS to Vacate Arbitration Award (Improper Parties)
3. Petition of Defendants HUNTINGTON BREAKERS to Vacate Arbitration Award (Bias of

Arbitrators)

4. Petition of Plaintiff C. W. DRIVER a partnership (hereinafter "DRIVER") to Confirm Arbitration Award

5. Motion of Plaintiff C. W. DRIVER for Severance of (1) Parties and (2) Second Amended Cross-Complaint Maguire, Toghia & Orbach by Everett W. Maguire and Steven L. Chesney appeared as attorneys for Plaintiff, respondent and Petitioner C.W. DRIVER, a partnership; and Callahan, McCune & Willis by George W. Coleman appeared as attorneys for Defendants, Petitioners and Respondents HUNTINGTON BREAKERS APARTMENTS, LTD., WILMORE CITY DEVELOPMENT,

INC., and JOSEPH P. MAYER III. No other parties to this action appeared.

On December 26, 1985, DRIVER timely filed its verified Complaint (Foreclose of Mechanic Lien) and Petition to Compel Arbitration and Stay Action Pending Arbitration against HUNTINGTON BREAKERS and other parties hereto. (The original of said verified Complaint and Petition is contained in the court's file in this action.)

On February 13, 1986, DRIVER filed in this action a verified Plaintiff's First Amended Petition to Compel Arbitration and Stay Court Action Pending Arbitration. (The original of said First Amended Petition is contained in the Court's file in this action.)

On March 13, 1986, after hearing

Plaintiff's first Amended Petition to Compel Arbitration and Stay Court Action Pending Arbitration, the Court issued a Minute Order stating:

> "Plaintiff's Petition to Compel Arbitration and Stay Court Action Pending Arbitration is granted except as to the Guarantors. The Court rules that the Guarantors are not parties to the agreement to arbitrate and action is stayed as to the Guarantors." (Exhibit "D" to the HUNTINGTON BREAKERS' Petition to Vacate Arbitration Award (Illegal Contract), and

Exhibit "5" to DRIVER's Verified Petition to Confirm Arbitration Award.)

The order granting arbitration was based upon Article 7.9 of the General Conditions that are referred to in and are a part of the Standard Form of Agreement Between Owner and Contractor (referred to in Defendants HUNTING BREAKERS' Petition as the "AIA Form Agreement," Exhibit "B" thereto and Exhibit "1" to DRIVER's Verified Petition to Confirm Arbitration Award.) which provide that all claims, disputes and other matters in question between the parties thereto shall be decided by arbitration in accordance with the Construction Industry Arbitration Rules of the American Arbitration Association.

The matter was arbitrated before the American Arbitration Association, Construction Industry Arbitration Tribunal, and the appointed arbitrators made their award dated October 4, 1990. (Exhibit "A" to HUNTINGTON BREAKERS' Petition to Vacate Arbitration Award (Illegal Contract) and Exhibit "9" to DRIVER's Verified Petition to Confirm Arbitration Award.)

The Court, having considered the moving and opposing documents on each of the above-listed petitions and motion, and having heard and considered oral argument on the Petition to Vacate Arbitration Award (Illegal Contract), makes the following statement of decision and orders thereon:

1. The Petition of Defendants HUNTINGTON BREAKERS APARTMENTS,

LTD., WILMORE CITY DEVELOPMENT and JOSEPH P. MAYER III to Vacate Arbitration Award (Illegal Contract) is granted, with respect to the following relief sought in the prayer of that petition:

(a) The award of the arbitrators dated October 4, 1990 is vacated and declared void;

(b) The Court finds that those portions of the contract document entitled "Guaranty and Indemnity Agreement" (Exhibit "C" to Defendants' Petition) that obligate the parties making that agreement to the payment of any contractor-construction costs over and above the $8.6 million guaranteed maximum cost stated

in the AIA Form Agreement constitute an illegal contract and are unenforceable.

(c) The Court finds that the Arbitration Award was based in part upon those portions of the Guaranty and Indemnity Agreement described above that are illegal and unenforceable.

2. Defendants HUNTINGTON BREAKERS' Petition to Vacate the Arbitration Award (Bias of Arbitrators) is now moot and is ordered off calendar.

3. Defendants HUNTINGTON BREAKERS' Petition to Vacate the Arbitration Award (Improper Parties) is now moot and is ordered off calendar.

4. Plaintiff DRIVER's Petition to Confirm the Arbitration Award is denied.

5. Plaintiff DRIVER's Motion for Severance of (1) Parties and (2) Second Amended Cross-Complaint is denied in its entirety.

Dated: July 12, 1991

/s/ ROBERT A. KNOX
Judge of the Superior Court